IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED: 05/10/2004

CORAM

THE HONOURABLE MR.JUSTICE P.D.DINAKARAN
AND
THE HONOURABLE MR.JUSTICE S.R.SINGHARAVELU

T.C.No.255 of 2004
and
T.C.Nos., 256 to 258 of 2004
and
T.C.M.P.Nos.175 to 177 of 2004

Commissioner of Income Tax .. Appellant

-Vs-

M/s.Annamalai Finance Ltd.
Coimbatore. .. Respondent

PRAYER: Against the order of the Income Tax Appellate Tribunal Madras 'A' Bench, dated 23.1.2003 in I.T.A.Nos.99, 103, 100, and 101/M/02 respectively.

!For Appellant : Mr.J.Narayanasamy
Junior Standing Counsel
for Income Tax Cases

^For Respondent : ---

:JUDGMENT
(Judgment of this Court was delivered by P.D.DINAKARAN,J.)

These appeals are directed against the common order dated 23.1.2003 of the Income Tax Appellate Tribunal, Madras 'A' Bench, made in I.T. A.Nos.99 to 101 and 103/M2/02, with reference to the assessment years 1992-93, 1993-94, 1994-95 and 1998-99.

2.1. In brief, the assessee-company is a non-banking financial company engaged mainly in the business of hire purchase and equipment leasing. After completion of the original assessments for the assessment years 1992-93, 1993-94, 1994-95, notices were issued by the Assessing Officer for reopening the assessments of the respondent/assessee on the ground that income has escaped assessment for the said three assessment years.

2.2. The Assessing Officer, during the course of the reassessment, by

assessment order dated 23.3.2001 for the assessment year 1992-93; and by assessment order dated 26.3.2001 for the assessment years 1993-94, 1994-95 and 1998-99,
(i) found that the change of method of accounting of overdue charges from mercantile basis to cash system was not justified and therefore, added overdue interest on mercantile basis;
(ii)rejected the claim of the respondent/assessee with reference to 1 00% depreciation on bottles purchased in bulk and leased out to others;
(iii)100% depreciation on steel rollers purchased and leased back to the same persons by the respondent during the assessment year 1993-94 and 1994-95 was also rejected;
(iv) the issue of cost under Section 43(1) of the Income Tax Act (for brevity "the Act") of the assets purchased and leased back during the assessment year 1994-95 was also rejected;
(v) the interest was levied for the delay in filing the revised return under

Section 234A of the Act; and
(vi)the higher depreciation on vehicles leased out as claimed by the respondent/assessee was also rejected.

2.3. Aggrieved by the said assessment orders of the Assessing Officer, the respondent/assessee preferred an appeal before the Commissioner of Income Tax (Appeals), who by an order dated 14.12.2001 upheld the assessment order of the assessing officer with respect to the inclusion of overdue charges to the income for all the four assessment years. The Commissioner also confirmed the addition of the differential depreciation made by the assessing officer for the assessment years 1993-94 and 1994-95 in respect of bulk leasing of steel rollers. However, he held in favour of the assessee with reference to 100% depreciation on the bottles, and also higher depreciation rate on vehicles leased out.

2.4. While the respondent/assessee preferred appeals with reference to the inclusion of the overdue charges on mercantile basis, the revenue preferred independent appeals against the allowing of 100% depreciation on the bottles and steel rollers, and also higher depreciation rate on vehicles leased out.

2.5. All the appeals were heard jointly by the Tribunal and disposed of by a common order dated 23.1.2003 allowing the appeals preferred by the assessee and dismissing the appeals preferred by the revenue. Hence, the revenue has preferred these appeals on the following substantial questions of law:
(i) Whether in the facts and circumstances of the case, the Tribunal was right in holding that the assessing officer did not have the jurisdiction to reopen the assessments for the assessment years 1992-93, 1993-94 and 1994-95?
(ii) Whether in the facts and circumstances of the case, the Tribunal was right in entertaining the assessee's objection to the jurisdiction of the assessing officer, which had not been raised at any earlier stage?

(iii) Whether in the facts and circumstances of the case, the Tribunal was right in upholding the action of the assessee in changing the method of accounting of overdue interest alone on a cash basis, when the system of accounting of the assessee was mercantile?
(iv) Whether in the facts and circumstances of the case, the Tribunal was right in allowing 100% depreciation on bottles purchased in bulk by the assessee and leased out to others?
(v) Whether in the facts and circumstances of the case, the Tribunal was right in allowing 100% depreciation on steel rollers which were purchased from and leased back to the same party?
(vi) Whether in the facts and circumstances of the case, the Tribunal was right in holding that the apparent consideration should be accepted by the assessing officer as the cost in a sale and lease back transaction, although the amounts specified as lease amounts were not received by the assessee?
(vii) Whether in the facts and circumstances of the case, the Tribunal was right in holding that no interest under Section 234A can be charged for delay in filing the return in response to notice under Section 148, as the original return was on file all the time?
(viii) Whether in the facts and circumstances of the case, the Tribunal was right in holding that leased out commercial vehicles are eligible for higher rate of depreciation?

3. After hearing the learned counsel for the appellant/ revenue and perusing the orders of the authorities below, we are inclined to pass the following order on the above substantial questions of law.

4.1. Questions (i) to (iii):
Question (i): - Whether in the facts and circumstances of the case, the Tribunal was right in holding that the assessing officer did not have the jurisdiction to reopen the assessments for the assessment years 1992-93, 1993-94 and 1994-95?

Question (ii): - Whether in the facts and circumstances of the case, the Tribunal was right in entertaining the assessee's objection to the jurisdiction of the assessing officer, which had not been raised at any earlier stage?

Question (iii): - Whether in the facts and circumstances of the case, the Tribunal was right in upholding the action of the assessee in changing the method of accounting of overdue interest alone on a cash basis, when the system of accounting of the assessee was mercantile?

4.2. A reference to the following admitted facts are relevant to deal with questions (i) to (iii), referred to above.

4.3. It is not in dispute that the respondent/assessee has fully and truly disclosed all material facts necessary for completing the assessments for the impugned assessment years 1992-93, 1993-94 and 1994-9 5 under Section 143(3) of the Act.

4.4. The period of limitation applicable to the reopening the assessments concluded under Section 143(3) of the Act for the assessment years 1992-93 and 1993-94 would be the period of four years prescribed in the proviso to Section 147 of the Act. In these two cases, the notices under Section 148 of the Act have been issued after the expiry of the four years from the end of the assessment years 1992-93 and 19 93-94. For the purpose of clarity, in respect of assessment year 199 2-93, if at all necessary, should have been issued on or before 31.3.1997, whereas, in fact, the notice was issued only on 5.3.1999. Similarly, in the case of assessment year 1993-94, notice under Section 1 48 of the Act should have been issued on or before 31.3.1998, whereas it was issued only on 5.3.1999. Therefore, apparent on the face of the record, it could be seen that the notice for the two assessment years 1992-93 and 1993-94 was issued after the expiry of the period of four years from the end of respective assessment years, violating proviso to Section 147 of the Act.

4.5. With reference to the jurisdiction to reopen the assessment for the year 1994-95, the assessing officer proposed to reopen the assessment for the year 1994-95 purely based on the change of opinion, namely the change in the method of accounting of overdue interest on cash or actual receipt basis, when the assessee was following mercantile system of accounting.

4.6. In COMMISSIONER OF INCOME TAX v. MATCHWELL ELECTRICALS (I) LTD, [2003] 263 ITR 227, a Division Bench of the Bombay High Court held that the change of method of accounting is permissible in law. In the said case, the assessee was engaged in the business of manufacturing electrical appliances. It followed the accounting year ending September, 20. The assessee was also engaged in exporting its products. The assessee received cash assistance and duty drawbacks from the Government of India. Prior to the assessment years 1977-78 and 1978-79, the assessee was accounting for receipts of cash assistance and duty drawbacks on the mercantile basis as its accounts were maintained on the mercantile basis. In revised returns for these years cash assistance and duty drawbacks were accounted on the cash basis. The Assessing Officer held that the assessee could not maintain a mixed system of accounting for different types of income. The Commissioner, however, held that the change in the method of accounting was bona fide and no loss was sustained by the Revenue. This was upheld by the Tribunal. The matter was taken on reference to the High Court. The Division Bench of the Bombay High Court held that the view of the Tribunal was justified in law holding that the export of duty drawback and cash assistance from the Government was assessable in the hands of the assessee on receipt basis and not on accrual basis.

4.7. It is a settled proposition vide the decision a Division Bench of the Calcutta High Court in HELA HOLDINGS PVT. LTD v. COMMISSIONER OF INCOME TAX, [2003] 263 ITR 129 that the assessee is entitled to change his regular method of accounting by another regular method. It would be open to the assessee to produce records and show that it had followed such changed accounting method in the subsequent years. In the said decision, the Calcutta High Court also laid the following general principles regarding tax avoidance and tax evasion, while dealing with the validity of the change in method of valuation, change in accordance with accounting practice and change followed

in subsequent years. The general principles are:
(i) the distinction between tax evasion and tax avoidance is still prevalent.
(ii) generally speaking, tax evasion is the result of such things as illegality, suppression, misrepresentation and fraud.
(iii) tax avoidance is the result of actions taken by the assessee, none of which is illegal or forbidden by the law in itself and no combination of which is similarly forbidden or prohibited.
(iv) the permissibility of a tax avoidance, will fall to be decided, when and only when, on the basis of the facts and transactions truly and correctly disclosed by the assessee, a point of law arises, whether on a certain reasonable construction of one part of the taxing statute, as applied to the assessee's case, tax which would otherwise be payable by the assessee, becomes not payable in the case in hand.
(v) When the court is faced with a task of construction in the above manner, the court is not bound to make the construction in favour of the assessee merely on proof by the assessee, that it has entered into no illegality and made no prohibited transaction.
(vi) the court would have to assess, in the facts and circumstances of each case, upon general principles of conscience and justice, whether the arrangement of affairs by the assessee, so as to cause the possibility of a reduction of tax incidence, can fairly be permitted to the assessee, as a genuine and legal means of tax reduction, employed by it in a commercial fair sense, or whether allowing the assessee to earn the reduction, in the facts and circumstances of the particular case, is opposed to the public policy of not encouraging citizens to engage themselves in dealings and transactions designed primarily for the purpose of non-payment of tax only.
(emphasis supplied)
4.8. In the instant case, the learned counsel for the revenue is not in a position to demonstrate or satisfy us that due to the change of accounting method adopted by the respondent/assessee, which is permissible in law as per the ratio laid down in (i) COMMISSIONER OF INCOME TAX v. MATCHWELL ELECTRICALS (I) LTD, [2003] 263 ITR 227; and (ii) HELA HOLDINGS PVT. LTD v. COMMISSIONER OF INCOME TAX, [2003] 263 ITR 129 , the revenue suffered any loss or such a change of methodology attracts tax evasion. Concededly, there is no finding to that effect in the assessment order or in the order of the Commissioner of Income Tax (Appeals).

4.9. The change of method of accounting of overdue charges from mercantile basis to cash system, method of accounting, as followed by an assessee, does not create any income; but the method of accounting only recognizes income. Therefore, either to apply accrual system or cash system, recognition of income is a paramount factor. In the present case, the disputed amount is the overdue charges receivable by the assessee from various parties on the basis of hire purchase and lease agreements. As per the terms of agreements, overdue charges are payable by the parties concerned to the assessee when they make defaults in paying the instalments as per the schedule of payments. When the instalment itself is overdue, is not collected, there is no basis for making out a case that the additional overdue charges payable by the parties would be collectible with certainty. The terms of the agreements which enable the assessee company to demand overdue charges is only an enabling provision and that enabling provision does not guarantee the

collection of overdue charges. It only gives a cause of action to the assessee. In such cases it is very difficult to recognize income against overdue charges.

4.10. We are, therefore, of the considered opinion that the Tribunal has rightly deleted the additions made towards overdue charges, acknowledging the change of method of accounting of overdue interest alone on cash basis.

4.11. In the course of reassessment, as held by the Division Bench of the Kerala High Court in COMMISSIONER OF INCOME-TAX v. SIVA TRADERS, [2002] 255 ITR 77, the Income Tax Officer is obliged to satisfy himself as to whether

the materials produced by the assessee and available on record, had any rational connection or live link for the formation of the requisite belief that the income chargeable to tax has escaped assessment.

4.12. A Full Bench of the Delhi High Court in C.I.T. v. KELVINATOR OF INDIA LTD., [2002] 256 ITR 1, interpreting the powers of the Income Tax Officer with respect to reassessment, held that a mere change of opinion cannot form a basis for reopening the completed assessment and further held that when a regular order of assessment is passed under Section 143(3) of the Act, a presumption can be made that such an order has been passed on application of mind. It is well known that a presumption can be raised to the effect that in terms of Section 11 4(e) of the Indian Evidence Act, judicial and official acts have been regularly performed. If it be held that an order which has been passed purportedly without application of mind would itself confer jurisdiction upon the Assessing Officer to reopen the proceeding without anything further, the same would amount to giving a premium to an authority exercising quasi judicial function to take benefit of its own wrong. Hence, it is clear that section 147 of the Act does not postulate conferment of power upon the Assessing Officer to initiate reassessment proceedings upon a mere change of opinion.

4.13. Accordingly, the questions (i) to (iii) are answered in affirmative, against the revenue and in favour of the assessee.

5.1. Question (iv): Whether in the facts and circumstances of the case, the Tribunal was right in allowing 100% depreciation on bottles purchased in bulk by the assessee and leased out to others?

5.2. This question is settled by a decision of this Court in FIRST LEASING CO. OF INDIA LTD. v. COMMISSIONER OF INCOME TAX, [2000] 244 ITR 238, wherein this Court held that each bottle was an independent unit and was not dependent for its user on the availability of other bottles whether empty or filled. The use of one bottle was not interconnected with the use of other bottles. Since each bottle was an individual unit and all bottles together did not constitute a single integrated unit depreciation under the proviso to Section 32(1)(ii) of the Act was allowable. Even in the instant case, the issue is relating to the allowance of 100% depreciation on each bottle and the said decision squarely applies. That apart, the case of the assessee is also

supported with another decision in COMMISSIONER OF INCOME TAX v. ALAGENDRAN FINANCE LTD., [2003] 264 ITR 269.

5.3. This question is also answered in affirmative against the revenue.

6.1. Question (v): Whether in the facts and circumstances of the case, the Tribunal was right in allowing 100% depreciation on steel rollers which were purchased from and leased back to the same party?

6.2. With regard to 100% depreciation in the case of steel rollers, an attempt was made by the learned counsel for the appellant that 100 % depreciation cannot be allowed in the case of steel rollers, because the ratio in the case of FIRST LEASING CO. OF INDIA LTD. v. COMMISSIONER OF INCOME TAX, referred supra, dealt with only leasing out of bottles which are valued below Rs.750/-. He further contended that the ratio in COMMISSIONER OF INCOME TAX v. ALAGENDRAN FINANCE LTD., [2003] 264 ITR 269, which deals with depreciation on centering sheets is also not applicable to the facts of the case, as Steel Rollers cost more than Rs.5000/-.

6.3. The Apex Court in COMMISSIONER OF INCOME TAX v. SHAAN FINANCE P. TD., [1998] 231 ITR 308 held that where the business of the assessee consists of hiring out of machinery and where the income derived by the assessee from such hiring is business income the assessee must be considered as having used the machinery for the purpose of its business. This position was reiterated by the Supreme Court in COMMISSIONER OF INCOME TAX v.

MAHARASHTRA APEX CORPORATION LTD, [2002] 254 ITR 98, and also the decision of this Court in COMMISSIONER OF INCOME TAX v. MADAN AND CO., [2002] 254 ITR 445.

6.4. We are, therefore, of the firm opinion that the Tribunal was right in granting 100% depreciation on steel rollers, and accordingly, we answer this question in affirmative in favour of the assessee and against the revenue.

7.1. Question (vi): Whether in the facts and circumstances of the case, the Tribunal was right in holding that the apparent consideration should be accepted by the assessing officer as the cost in a sale and lease back transaction, although the amounts specified as lease amounts were not received by the assessee?

7.2. Strictly speaking, "apparent consideration", as held by the Bombay High Court in POLYCON PAPER LTD. v. UNION OF INDIA, [2002] 253 ITR 182, would mean the whole or part of the consideration for such transfer, which is payable on any date or dates falling after the date of such agreement for transfer, and the value of such consideration payable after such date

shall be deemed to be discounted value of such consideration as on the date of such agreement or transfer, determined by adopting such rate of interest as

may be prescribed in this behalf.

7.3. Therefore, unless and until there are reasons to believe that the cost in a sale or an amount in a lease back transaction, as specified, was received, but not disclosed, we do not see any error, on the part of the Tribunal, in accepting the apparent consideration.

7.4. This question is, therefore, answered in affirmative and against the revenue.

8.1. Question (vii) - Whether in the facts and circumstances of the case, the Tribunal was right in holding that no interest under Section 234A can be charged for delay in filing the return in response to notice under Section 148, as the original return was on file all the time?

8.3. Since, when the very reopening of the case for the assessment years is based on change of opinion and on irrelevant, illogical and unsustainable reasons, without any jurisdiction, the question of demanding interest under Section 234A of the Act does not arise.

8.4. This question is also answered in affirmative, against the revenue.

9.1. Question (viii): Whether in the facts and circumstances of the case, the Tribunal was right in holding that leased out commercial vehicles are eligible for higher rate of depreciation?

9.2. This issue is settled by a decision of the Delhi High Court in COMMISSIONER OF INCOME TAX v. BANSAL CREDITS LTD., [2003] 259 ITR 69. On a plain reading of Section 32 of the Act and entry III(2)(ii) in Appendix I to the Rules, it is clear that it is the end user of the specified asset which is relevant for determining the percentage of depreciation. Section 32 of the Act requires that the asset should be used for the purpose of the assessee's business and the entry in the Appendix refers to the user it should be put to. Once it is accepted that the leasing out of the vehicles is one of the modes of doing business by the assessee and in fact the income from such leasing is treated as business income of the assessee, it would be clearly contradictory in terms to hold that the vehicles in question were not used wholly for the purpose of the assessee's business. The Delhi High Court held that the assessees, which were engaged in the business of leasing out commercial vehicles, were entitled to depreciation at the higher rate of 40 per cent as provided in item III(2)(ii) of Part A of Appendix I to the Income Tax Rules, 1962.

9.3. This Court in COMMISSIONER OF INCOME TAX v. MADAN & CO., [2002] 254 ITR 445, explaining reason for eligibility for higher rate of depreciation in the case of leased out vehicles, while interpreting Entry III(2)(ii) of Appendix I, namely "Motor buses, motor lorries and motor taxis used in a business of running them on hire", held as follows:
"Owners of vehicles who used it for their own purposes are allowed to claim depreciation at the normal rates. Owners of vehicles mentioned in the entry

when they allow it to be used for a price are allowed to obtain a higher rate of depreciation. The distinction is based upon the fact that a person who obtains the temporary right to use of the vehicle on payment of a charge price is likely to, by the nature of his user, such user being for the purpose of the hirer and not the owner, depreciate the value of the vehicle faster.

All such vehicles, which are so used, are likely to undergo a little more rough use than vehicles owned by and used for the personal purposes of the owner. It is in recognition of that fact of the depreciation occurring at a faster rate for such vehicles that the law provides for the higher rate of depreciation.

The fact that the assessee here chose to lease out the vehicle does not on that score disentitle the assessee to claim the benefit of the higher depreciation. The lease of the vehicle enables the lessee to have possession of the vehicle, and have the right to use the vehicle as the lessee wishes, subject to the terms of any contract between the parties. The lessee during the period of user is also likely to have to maintain the vehicle subject to the terms of the contract between the parties. For having the benefit of the user of the vehicle, the lessee is required to pay a price which is the lease amount, whether called rent or hire charges. The terminology used for describing the payment makes no difference in substance. What is paid is an amount in consideration of the right obtained from the owner to have the use of the vehicle for the benefit of the lessee for the stated period, and, or the stated purpose, whether or not by employing his own drivers, and whether or not also undertaking to maintain the vehicle during the period of the lease or hire.

The word "hire" used in this entry is only meant to denote that the use of the vehicle is not by the owner himself for his own purposes, but it is given to another for use for a limited period of that other for a consideration. For the purpose of this entry there is no qualitative difference between lease of the vehicle for a specified period for consideration and letting the vehicle on hire for short duration on payment of hire charges."

9.3. Applying the ratio laid down in the above decisions, viz., (i) COMMISSIONER OF INCOME TAX v. BANSAL CREDITS LTD., [2003] 259 ITR 69; and (ii) COMMISSIONER OF INCOME TAX v. MADAN & CO., [2002] 254 ITR 4 45, this question is answered in affirmative, in favour of the assessee and against the revenue.

These appeals are disposed of accordingly. Consequently, connected miscellaneous petitions are closed.

Index : Yes
Internet :Yes

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